American Telephone and Telegraph Company

1972 Annual Report

"There is in my mind no conflict among our responsibilities to the public, to our share owners and to our employees. Fundamentally, however, our business exists for no other reason than for the service it provides the public. That is why I say that our responsibility to investors places no greater obligation upon us than doing the very best service job we know how to do. We must earn our earnings and this your management pledges to do."

— John D. deButts, Chairman of the Board

The Annual Meeting of share owners will be held at 2 p.m. on Wednesday, April 18, 1973 in the Arie Crown Theatre, McCormick Place, Chicago, Illinois. Any persons who plan to attend the meeting should write to the Secretary of the Company for an admission card.

The financial results reported herein are for the American Telephone and Telegraph Company and its principal telephone subsidiaries, consolidated.

If you need further information:

—Financial statements of AT&T alone and annual reports of the Bell Telephone operating companies and of Western Electric, manufacturing and supply unit of the Bell System, are available on request.

—Also available is an Annual Statistical Report, intended for those desiring further data on our operations.

—Share owners who are blind may obtain the AT&T report in braille or on talking records.

Kindly address requests to the Secretary, American Telephone and Telegraph Company, 195 Broadway, New York, N.Y. 10007

The Company maintains stock transfer offices at 180 Fulton St., New York, N.Y. 10007 and also at: 185 Franklin St., Boston, Mass. 02107; 225 West Randolph St., Chicago, Ill. 60606; and 140 New Montgomery St., San Francisco, Calif. 94105

American Telephone and Telegraph Company

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Results in Brief

	1972	1971*
Earnings Per Common Share	$ 4.34	$ 3.92
Income	Millions	
Local Services	$10,363	$ 9,135
Toll Services	9,771	8,633
Other	1,218	1,111
	$21,352	$18,879
Expenses		
Operating	$13,518	$12,075
Taxes	3,807	3,314
Interest	1,495	1,288
	$18,820	$16,677
Net Income	$ 2,532	$ 2,202
Dividends Declared	$ 1,633	$ 1,486
Earnings Reinvested in the Business	$ 899	$ 716

**Restated (see Note (b) page 35.)*

On April 1, 1972, a new management team was elected to head the Bell System. John D. deButts (center) became Chairman of the Board. Robert D. Lilley (left) was named President, and William L. Lindholm, Vice Chairman of the Board.

Report of the Chairman of the Board

Dear Share Owner:

In 1972 the Bell companies did what they set out to do: improve service, improve efficiency, improve earnings.

Revenues rose 13 per cent and net income applicable to AT&T common shares over 10 per cent. Earnings per share were $4.34 vs $3.92 a year ago.

This earnings improvement didn't just happen. It was *made* to happen.

A rising economy helped, as did our growing mastery over service difficulties that have plagued recent years.

So, too, did the growing recognition on the part of regulatory authorities of our need to reprice our services at levels that reflect their cost and value today.

But the key factor in the year's outcome was the energy and intelligence with which Bell managers applied themselves to improving efficiency and controlling costs in every aspect of our operations.

In short, the Bell companies recognized that only by a significant improvement in earnings per share could the Bell System assure its ability—after three years of flat earnings—to finance on sound terms the very large construction programs it must undertake in the years ahead to meet the public's communications needs. Accordingly, from the year's outset the Bell companies made it their aim to demonstrate—promptly and convincingly—their ability to accomplish an earnings improvement that would warrant the continuing confidence of current investors in our business and the interest of new ones. The year's results fulfill that objective.

These results were not accomplished—and could not be—by headquarters edict. Rather were they the product of the efforts of thousands of Bell System managers who, seeing what needed to be done, committed themselves to goals that—like the Bell System's goals—were just a little more demanding than seemed reasonable at the outset. They wrote the record of the year's accomplishments that is set forth in these pages. And it is to them that this Annual Report is dedicated.

Perhaps the clearest measure of the year's advances in productivity is the fact that—with virtually no increase in employees—the Bell companies at year's end were handling a volume of business over 10 per cent higher than they were handling at the beginning.

It is now three years since an AT&T Annual Report first took note of the serious service difficulties that had developed in some places and the severe public criticism that ensued. At that time we said that no effort would be spared to set matters right.

And no efforts have been spared. While much remains to be done, what should be clear is that the general level of telephone service the Bell companies provide has been steadily improving. It is particularly gratifying to note that New York City, site of our most widely publicized difficulties, is generally in good shape. Wherever other service problems remain, we stand firm in our determination to correct them, too, as promptly as possible. In some areas where demand continues to accelerate at an extraordinarily rapid pace, this will doubtless prove to be an arduous, complex task. But, as I said at our Annual Meeting in the spring, our responsibility to investors places no greater obligation upon us than doing the very best service job we know how to do—and this your management pledges itself to do.

Recent years have seen a considerable increase in the scope and intensity of regulatory activity affecting our business. Partly this derives from the emergence of competition in the communications industry and the policy questions it raises. And partly it derives from our own need to seek authority for rate increases that will permit us to earn at levels sufficient to warrant the confidence of today's investors.

With respect to the degree to which competition should obtain in an indus-

try that owes its present advanced state of development and the low cost of its services to the shared use of common facilities, I expressed myself at some length at our Annual Meeting last April. Suffice it to say here what I said then. We do not intend to abdicate any sector of our business where we are convinced—and can by our performance prove—we can do a better job for the public than anybody else. In short, in whatever aspects of our business competition may be found to be in the public interest, we intend to be good competitors. But we shall vigorously oppose any proposition that, whatever advantage it may offer to a few, would impair or restrict our ability to serve the public at large or add to the costs of doing so. Share owners may be assured that in the gathering debate over the role of competition in communications our views will be vigorously represented.

But share owners—because they are customers as well as investors—are likely to be more immediately concerned with the rising cost of service.

In 1972 nearly all the Bell companies sought rate increases from the regulatory commissions in their territories, some of them for the second or third time in recent years. They did so in the face of a general stiffening of the public's resistance to price increases on every front and in full recognition of the risks of appearing to run at cross-purposes to the government's anti-inflation policy. But they did so because their responsibilities to their customers as well as their share owners afforded them no other choice.

That choice was dictated by an obligation that we, like other utilities, have no alternative but to meet. In good times and bad and regardless of whether costs are going up or down, it is our responsibility to meet public demand when and where it arises. What now requires us to seek higher rates at a time when price rises in the general economy are slowing is the continuing expansion of capacity required of us and the very large amounts of new capital it takes to finance that construction—$3.7 billion in 1972 alone.

No business is more committed to the fight against inflation than ours. It could hardly be otherwise in view of the arduous and protracted process it requires to gain regulatory approval of rate changes that reflect the costs we experience. That is why—down through the years—we have exerted every means to conserve capital and cut costs that sound management and advancing technology afford. When those efforts prove insufficient, however, we have no other recourse than to seek authority to reprice our services. To do otherwise would be to risk falling short of the service expectations of our customers and the earnings expectations of our investors.

Above I described the results of our 1972 applications for increased rates as generally heartening. That does not mean that we have not encountered disappointments in some jurisdictions. Even though our per share earnings are much improved, there still are places not paying their proper share of service costs. Where this is so we must continue to ask for rate increases. Indeed, in some places where regulators have been indisposed to recognize what appear to us to be today's financial realities, Bell company managers must of necessity consider carefully whether construction activity can be continued at current levels in the absence of the prospect of earnings sufficient to provide an adequate return on the new investment required.

It would be regrettable, it seems to me, if as a result of the often-heated contention that surrounds some regulatory proceedings the impression were to be conveyed that there is somehow an inevitable and irreconcilable conflict between the interests of our customers and the interests of our share owners. There is not. Good earnings and good service are inseparable objectives. To fall short of one is to risk losing both.

Most regulators, I am glad to say, understand this relationship. It is crucially important that the public understand it as well.

Nobody likes price increases. Reminded, however, of the fact that throughout the decade of the 60's tele-

phone rates stood firm while the prices of nearly everything else were going up, the public will, I believe, be ready to recognize the reasonableness of our needs. And I believe, too, that, presented with the facts, the public will be ready to recognize that to serve we must build and to build we must earn—and earn at levels that are competitive with investment opportunities in other businesses, regulated and unregulated. The alternative to our doing so is to acquiesce in that irreversible process that begins with inadequate capitalization and ends in deteriorating performance and the demoralizing appeals for public subsidy that have been the all-too-familiar history of some once-great businesses. Down that road the Bell companies are not ready to take even the first step.

To see that we do not, we shall continue to press vigorously in each regulatory jurisdiction for the opportunity to achieve the earnings growth we believe is necessary to assure the long-run vitality of this business and the service it provides the public. At the same time we shall neglect no opportunity to demonstrate through performance—by continuously enhancing the usefulness of our service and the efficiency with which we provide it—that we do in fact earn our earnings.

In conclusion, two personal observations:

First of all, it is my hope that share owners, as they turn the pages of this report, will recognize that what is recorded here represents but an all-too-cursory summing up of the year-long efforts of more than a million people. Some of them work at switchboards, some in offices, some in factories. Some are stenographers and some technicians. Some compose computer programs and some spend their days exploring the remotest regions of science. What gives their diverse efforts a common purpose and direction, however, is the leadership provided by the thousands of Bell System managers whose responsibility it is to produce the results that, when the contribution of each has been added to all the others, will achieve the goals of our organization as a whole. In recent months I have been spending as much of my time as possible traveling among the Bell companies and meeting with managers of all levels. It is as much from my experience of these meetings as it is from the year's results themselves that I can state with confidence that—after difficult times—our business is on the move again. What is more, the competence and the can-do spirit that I encountered in these Bell managers wherever I have traveled confirms my conviction that it will keep on moving. You will meet some of them in the following pages.

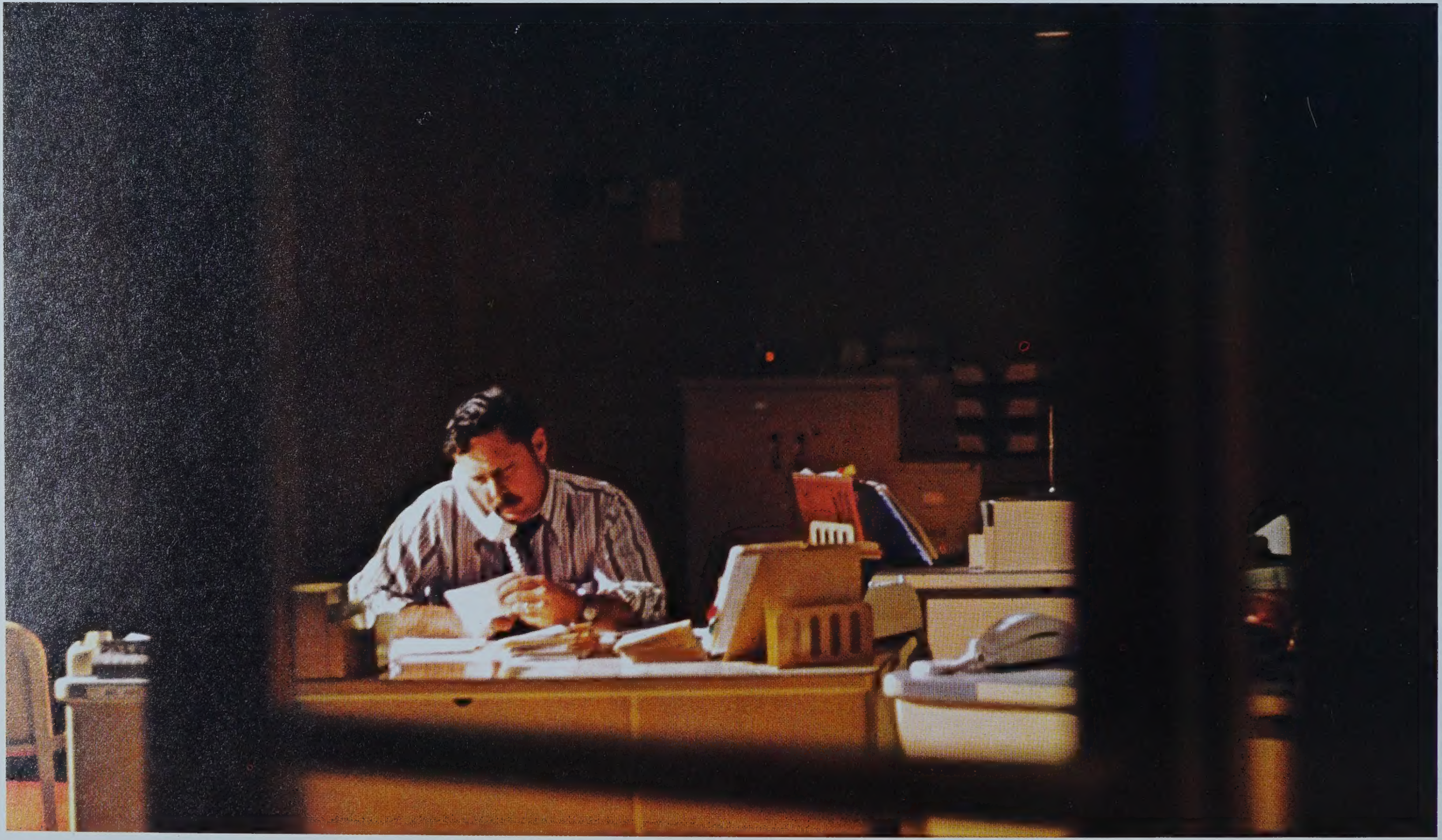
Finally, no account of the Bell System's progress in 1972 would be complete without acknowledging the profound contribution to that progress of the man under whose leadership we began the year and set its goals. On March 31, H. I. Romnes retired after a distinguished Bell System career of some 43 years, the last five of which he served as AT&T's chairman and chief executive officer. That the Bell System has emerged from a difficult period with its strength undiminished and its prospects bright we owe in no small measure to the integrity of his decisions and the steadfastness of his commitment to public service. Mr. Romnes, I am glad to say, continues as a director of our company.

John D. deButts

February 12, 1973

The Telephone Manager

The Bell System managers pictured in these pages are representative of the thousands more—in small towns and big cities, on construction sites, in switching offices, in factories and laboratories all across the country—to whom our business looks to coordinate and direct the resources required to meet its service and earnings goals. It is in large measure because they made these goals their own that the results reported in these pages were achieved—and it is to them that this report is dedicated. Shown here is Robert Chadwick, manager in Alliance, Nebraska (pop. 7,000).



In 1972 the Bell companies added 5.1 million telephones, more than in any single year in our history. Bell telephones in service totaled 105.3 million at year's end.

During the year, the Bell System handled 410 million messages per business day—22 million more than in 1971—and long distance calling increased by over 10 per cent.

From these indicators it is clear that 1972 saw an end to the economic slowdown that dampened Bell System growth in the two prior years. Indeed, at year's end there was no major sector of telephone growth—save one—that did not match or exceed—in some cases by a considerable margin—the growth trends we have experienced since the end of World War II. Particularly strong was the growth in residence extensions and in the number of telephones serving small businesses. Large business demand still lagged long-term trends but moved up significantly during the year.

Responding to stepped-up marketing efforts, more customers ordered premium telephones than ever before. For example, of the 28 million telephones the Bell companies installed last year, about 14 per cent were Trimline® telephones with their dials (or pushbuttons) in the handset. And Touch-Tone® telephones accounted for about four out of every 10 telephones added in the 6,740 exchange areas—out of a total of 15,650—where this service is available.

During the year we continued our efforts to acquaint our customers with the economies of dialing their own long distance calls and calling at off-peak hours—and more and more telephone users are responding to this encouragement. In 1972 about 79 per cent of long distance calls were customer-dialed and the new interstate rates that became effective early this year provide a further stimulus to this trend.

Overseas calling continues to grow at a rapid pace. In five years it has more than tripled and, if recent trends continue, it will triple again by 1977. By 1980 we expect to be handling 200 million overseas calls compared with 39 million in 1972.

We plan a further expansion of direct dialing by customers of overseas calls—a service already available in parts of the New York and Washington metropolitan areas and a few other locations. By the end of 1973, we anticipate that it will be available in parts of most major U.S. cities. We expect that it will further stimulate calling internationally just as it has domestically.

Operating Results

In 1972, over-all Bell System revenues increased 13 per cent and operating expenses 12 per cent. Operating taxes totaled $3.8 billion, of which well over half went to state and local governments. Interest charges on debt obligations amounted to $1.5 billion—a 15 per cent increase over 1971. The rate of earnings on capital was 7.7 per cent, compared to 7.4 per cent last year. Net income totaled $2.5 billion, of which almost $1.5 billion was paid in dividends to three million holders of common shares and $146 million paid or committed to holders of preferred shares. In August, the Directors voted to increase the quarterly dividend from 65 to 70 cents per common share, the seventh increase since 1958.

Construction

In 1972 the Bell System spent some $8.3 billion to expand, improve, replace or relocate its physical facilities—about three-quarters of a billion dollars more than we spent for like purposes in 1971. This expenditure enabled us to add 32 million circuit miles to our nationwide network of transmission facilities and enough new calling capacity in local exchanges to serve six cities the size of Cleveland.

In the course of the year we installed 118 electronic switching systems (ESS), bringing to 324 the number of such systems we have installed since the first one was cut into service in

"No question about it, we accomplished a lot in 1972. We improved service and reduced costs. Our entire work force today is more experienced and productive. The key to all this is the desire of the individual employee; our people—for the most part—want to do a good job. What we must continue to do is to provide a good work environment, good training, and the job will get done—and done well."
Joe Hunt, Assistant Vice President—Operations (Plant), AT&T

1965. In three years the number of telephones served by these fast-acting, versatile systems has climbed from 1.1 million to 6.2 million and we anticipate that a steady buildup in the pace of ESS production and installation will make its services available to fully half our customers by the mid-1980's.

We plan a like acceleration in the availability of the benefits of electronic consoles that enable operators to handle customer-dialed person-to-person, credit card, collect, third number and pay station calls much more expeditiously than they can from the traditional switchboards. At the end of 1971, some 7,800 of these consoles had been installed; by the end of 1972 there were over 11,000—in 82 places, their services available to almost 33 per cent of our customers.

Of 1972's construction expenditures, $1.0 billion was invested in modernization projects, like ESS, aimed at providing better, more efficient service to the public.

Another $400 million was spent for plant relocation—to make way for highway construction, for example—and for replacement of facilities no longer fully serviceable, including those damaged by storm.

In this connection, the "bill" for the damages to telephone plant as a consequence of Tropical Storm Agnes came to some $32 million, of which about $18 million was for construction of plant to replace that destroyed by the storm.

It should be noted that the pace at which service was restored in this emergency —often under conditions of acute discomfort—provides renewed

evidence, if any were needed, of the value of Western Electric-telephone company teamwork and the vitality of the Bell System's tradition of service in emergencies. Most of the damage was centered in the territories of the Chesapeake & Potomac Telephone Companies, the Bell Telephone Company of Pennsylvania and the New York Telephone Company. We are confident, however, that had a like emergency occurred anywhere else in our territories, it would have been met with a like response.

Some $1.4 billion of 1972's construction budget was spent for "customer movement"—that is, putting in and taking out telephones as customers change their residence or business locations. The scale of this activity remains astonishing even to us. To "gain" the five million telephones we added to our lines in 1972, we installed 28 million, removed 23 million.

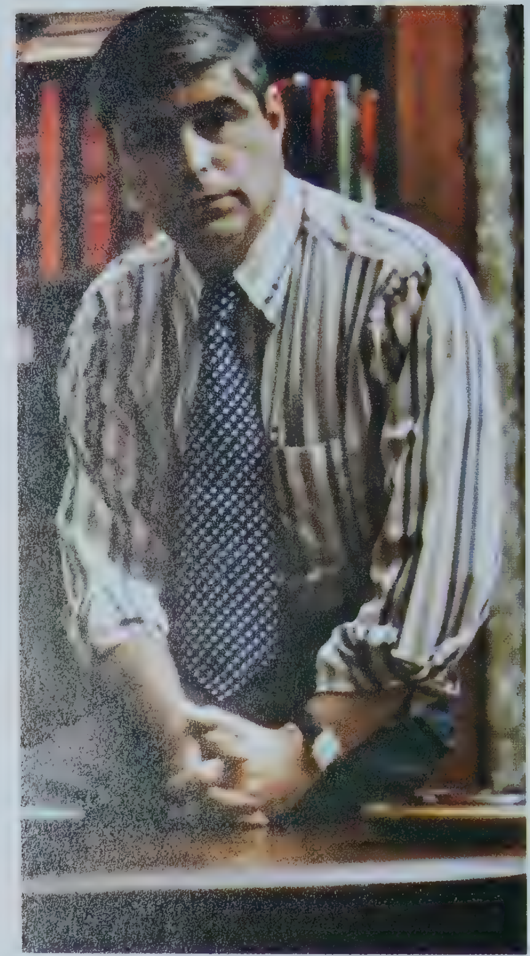
But by far the largest portion of our 1972 construction expenditures—$5.5 billion—was spent for growth, current and prospective. In this connection, it should be noted that we do not expect to see the steep rises in construction costs that have marked the recent past continued into the years immediately ahead. That does not mean that we foresee any significant slackening of demand for our services. It does mean that we see hope for some slackening of the pace of inflation, which has added some $5.5 billion to the cost of our construction over the past five years. What may be more significant is that the record-breaking construction outlays of recent years, undertaken as they were in the face of lagging demand and albeit at a cost in terms of current earnings, now serve us in good stead as we experience once again the strong growth in demand we knew would one day come and for which we knew we must be ready.

Where do the Bell System's construction dollars go?

During 1972, some $2.5 billion went to pay for the telephone company engineering and employment costs involved. Some $2.1 billion went to outside suppliers and contractors. And $3.7 billion went to the Western Electric Company for the communications hardware—the wire and cable, the switching machines and the transmission systems—it makes for the Bell telephone companies. But Western Electric, in turn, looks to thousands of suppliers, large and small, throughout the United States, for raw materials and components it uses in its own manufacture. Thus the Bell System's construction program makes a major contribution to the growth of the economy it aims to serve.

"The vital ingredient in the success of any request for higher rates, of course, is a high quality of service. But in addition, a telephone company has to demonstrate to the public that it is attempting to run the business with integrity and efficiency. No less important is a solid reputation for delivering on your promises and commitments."

John Hayes, Assistant Vice President—Revenue Requirements, Southwestern Bell



"Improved earnings is a two part thing. First we have to keep striving for internal efficiency. When this doesn't provide adequate earnings, though, we have to seek rate increases. On both counts, I think we've turned the corner. Certainly the efforts put forth by Bell System people to meet these goals and get the business moving in the right direction have been important factors in our success in achieving this year's earnings results."
Bill Burns, Assistant Treasurer, AT&T

Western Electric's performance last year, its contributions to the quality and economy of telephone service, the magnitude of its manufacturing and supply operations, were again impressive by any measure. The company produced 4.8 million lines of dial central office equipment and set new records in the production of telephone sets (over 10 million) and exchange cable (312 billion conductor feet). Moreover, the company achieved its manufacturing and service objectives without any increase in the prices of its products, which today average about 65 per cent of the prices of like products from other manufacturers. Rigorous expense control, record achievements in engineering cost reduction, and improvement in over-all productivity were the principal factors contributing to this success.

Western Electric sales last year amounted to $6.55 billion, compared to $6.05 billion in 1971.

Financing

Of the $3.7 billion in new money the Bell companies required to finance their construction last year, $2.5 billion was obtained through the public sale of debt securities by AT&T and 12 of its operating subsidiaries, and about $200 million from bank loans. Another $1.0 billion was obtained through a private placement consisting of $625 million of cumulative nonconvertible preferred stock and $375 million in 25-year notes. This private placement was negotiated in 1971 and the proceeds were taken down during the first half of 1972.

Interest costs on 1972 debt issues ranged from 6.47 to 7.75 per cent. At the end of the year, the average interest cost of all Bell System long-term debt outstanding stood at 6.15 per cent—up from 4.46 per cent just five years ago—and the ratio of debt to the Bell System's total capital was 47 per cent.

We do not believe that this ratio should go much higher.

To help assure that it does not, the Bell System is explicitly setting out to accomplish a further improvement in earnings per share sufficient to warrant a market price for AT&T shares that will permit an offering of common equity on terms that will maintain the integrity of the investment of existing share owners. While a sufficient range of financing alternatives remains to us to preclude the necessity to undertake such an offering in the near term, clearly our efforts must be addressed to advancing the day when it will be practical to do so.

It is to this end that we continue unremittingly our efforts to improve earnings through improving efficiency. And it is to this end that we continue—

because we must—our efforts to reprice our services at levels that will provide us the opportunity to achieve earnings sufficient to make it feasible to undertake the common equity offerings that maintaining a sound financial structure and a top credit rating so clearly require.

In a move designed mainly to produce tax benefits for both AT&T and the New England Telephone and Telegraph Company, the parent organization tendered late in the year an exchange offer for additional stock in the New England firm that increased AT&T's ownership from over 71 per cent to 85.4 per cent. The exchange ratio was 8/10 of one AT&T share for one New England share.

Telephone Rates

In 1972 regulatory authorities in 36 jurisdictions authorized rate changes that will add approximately $700 million to Bell System annual revenues. In addition the Federal Communications Commission in late November authorized the company to file rate increases for its interstate

"Day in and day out, you need to reappraise where you're going and how well you're spending your dollars. But you should not do anything in your zeal for cost controls that will affect the business in the long run."
Betty Hunt, Toll Assistance Department Manager, Pacific Telephone

services sufficient to produce $145 million in additional income before Federal Income Tax. Most of these rate changes became effective in January of this year and apply principally to operator-assisted calls, reflecting their higher costs, and to customer-dialed calls during the day-rate periods. Even with these increases, the level of interstate telephone rates today is below the level of 1953.

It is heartening to note that in the course of the year a number of states authorized rates of return approaching the level that we believe is desirable to assure sound financing of the very sizable construction program we must carry out to meet the public's growing communications needs under today's conditions. And in its November ruling, the FCC, while it authorized rate increases sufficient to produce a rate of return of 8.5 per cent on our interstate services, at the same time explicitly recognized that a rate of return of 9 per cent, assuming it can be achieved through improved efficiency, would be appropriate under today's conditions. This, we are confident, we can accomplish.

Nonetheless there remain many states in which the rate of return the Bell companies are earning on their invested capital is well below the level needed to meet today's competitive financing conditions, thereby placing our ability to provide continuing good service in these places in some jeopardy. In these jurisdictions we have no alternative but to press—and press hard—for rate increases that will produce the sustained earnings growth that is needed to support

"We were hard hit by Tropical Storm Agnes. Some of our people were wiped out—they had nothing left but the clothes on their backs. Yet they came to work anyway. The response was tremendous. I was impressed that people put in the kind of hours they did. That told me something; if it was strictly for compensation, I don't think they'd have put forth that kind of effort."

Bob Masoner, District Commercial Manager, Wilkes Barre, Bell of Pennsylvania

continuing service growth.

Down through the years the Bell telephone companies have pursued a pricing policy aimed broadly at encouraging the development of their services and stimulating their usage. Installation charges, for example, have traditionally been kept low so that more and more people might enjoy the benefits of service. Today, however, universal service, the aim of our business from its beginning, has been virtually achieved. At the same time, customer requirements—and therefore the costs they occasion—have become more and more diverse. Accordingly the telephone companies are moving toward a restructuring of their charges that will match the rates for particular services more directly to their costs. For example, we are persuaded that we should recover the costs of moving, changing and installing telephones from the people who occasion these costs rather than from monthly charges that are applicable to all our customers, whether they move or not. Already regulatory authorities in a number of states have approved increases in installation charges that represent a step in this direction.

Another example: today, nobody pays for Directory Assistance—or, more realistically, everybody does. On the average about 50 cents of the residence customer's basic monthly charge goes to pay for Directory Assistance service. And yet a sizable majority of Directory Assistance calls are made by a relatively small percentage of customers. Accordingly it has been proposed that a charge be instituted for DA calls exceeding a basic allowance that would meet the needs of most customers. In a number of places where this proposal has been broached, it has been greeted by strong protests based, we are convinced, on misunderstanding. Its aim is *not* to increase revenues but simply and only to remove the burden of cost from the general body of customers and assign it to those who benefit from a disproportionate use of this service. We believe that the public will in time come to see the fairness of this proposal and we intend to seek authority to implement it.

Again in the interest of more nearly matching prices to costs, a number of the telephone companies are studying rate plans that separate—in proportion to their costs—the charges for telephone instruments and their installation from charges for access to our network. Similarly, we have under development a restructuring of interstate private line rates that, taking advantage of the economies of scale our high capacity routes afford, will permit us to charge lower rates on these routes,

"People today don't respond positively to autocratic management. They want to know why. Once they know why, there is a 110 per cent commitment to doing an outstanding job. If we changed our management practices tomorrow and explained why, we'd have a hundred supervisors scrambling to get there."
Stanley (Pete) Clow, Vice President and General Manager — Kansas, Southwestern Bell

"Our people in North Dakota have really worked hard to provide the best telephone service we can provide. I believe our customers expect this and are willing to pay for it. Anything less is no bargain at any price. But I also know we can't give good service without good earnings."
Bill Stauffer, Vice President and General Manager—North Dakota, Northwestern Bell

somewhat higher rates elsewhere. This restructuring would represent the first departure from the principle of nationwide average pricing that has contributed so much to the development of communications in this country. The goals of nationwide average pricing of private line services having been substantially achieved, it now seems appropriate to consider charges more directly related to costs.

It is now nearly five years since the Bell companies—in response to the FCC's ruling in the Carterfone case—filed tariffs permitting connection of customer-owned devices and systems to Bell System lines through suitable telephone company-provided interfaces. For some time now the FCC has been inquiring into the feasibility of a further liberalization of interconnection policy. More specifically, what is being explored is whether a system of "certification" of equipment suitable for connection to the telephone network might not provide an appropriate alternative to current interface requirements. We are cooperating fully in this inquiry and with the joint board of federal and state regulators that the FCC has asked for recommendations. At the same time we have made no secret of our concern about the long-run consequences of the division of responsibility for service that a certification system would necessarily entail and the consequences as well in terms of added costs to the average customer. Until these and related questions have been thoroughly explored, we do not believe a responsible determination can be made as to whether certification is or is not in the public interest.

Ahead in Service

Many Bell System innovations, like the transistor (invented at Bell Laboratories just over 25 years ago) and the Telstar communications satellites, have won acclaim from scientists and laymen alike. Thousands of others are virtually unknown outside the scientific community. (Bell Laboratories, for example, has produced over 15,000 patents since it was founded in 1925—more than one every working day.) Yet it is to the cumulative effect of these innovations—rather than to any single startling breakthrough—that we owe the steady advance of the communications art down through the years.

For example, demand for data communications continued to grow in 1972, and technological developments emerging from Bell Laboratories are enabling us to more than keep pace with the needs of this important market, the potentialities of which we recognized as long ago as 1958 when we introduced our first Dataphone® data sets. Thus, last year we sought FCC permission to con-

"People in Indiana—like everybody, everywhere, I guess—insist upon good service. They can be critical when they feel they're not getting it. So we teach our telephone operators to try to satisfy customer requests for assistance however out of the ordinary they may be. We think it's good for our customers—they're better served—and good for our operators—they feel more pride in being able to handle the out-of-the-ordinary call."

Bill Davis, District Traffic Manager, Indiana Bell

"What a job our people in New York have done. We've experienced the biggest turnaround in the history of any telephone company. Service is back. It has to be our greatest team effort ever."

Sal Barbera, Assistant Vice President—Network Operations, New York Telephone

struct a digital data system that by the mid-seventies will link almost a hundred cities. Thanks to a new technique called "Data-Under-Voice," or DUV, the digital system can be deployed and operated far more economically than once thought possible. The system will provide digital services at speeds that range up to 56 kilobits per second.

In another development reflecting advances in technology, AT&T requested FCC permission to move ahead with full-scale implementation of a new high-capacity mobile communications system. Through techniques that make highly efficient use of the frequency spectrum, the system would, for the first time, make available to all customers who wish it, a wide range of mobile communications services as good as regular telephone services.

The astonishing growth in overseas calling impelled us last year to seek authorization to lay new telephone cables of advanced design under both the Atlantic and the Pacific Oceans. In July, the FCC authorized AT&T and three international record carriers to construct a sixth transatlantic cable. TAT-6 will provide upwards of 4,000 two-way voice grade circuits—more than four times the capacity of TAT-5 which was completed two years ago. The new cable is scheduled for operation by early 1976.

Meanwhile, AT&T has requested FCC approval for construction of an 845-circuit cable between Hawaii and Okinawa to supplement existing links to the Far East. It would connect with a cable we have proposed from California to Hawaii, which has been under FCC consideration for over a year.

AT&T's undersea cable proposals are in keeping with our advocacy of a roughly fifty-fifty mix of cable and satellite circuits as the best assurance of continuity of service in the event of a failure in one mode or the other.

In December the FCC gave a go-ahead to the company's proposal to use communications satellites as an integral part of its network of facilities serving the U.S. The Communications Satellite Corporation (Comsat) will provide the space segment of the proposed system.

While we are gratified by the Commission's go-ahead, we remain concerned by the restrictions it places on our use of satellites that would bar us—for a period of three years—from using satellites for private line services. An important matter of principle is involved here. We believe that it is technically and economically unsound to prevent the Bell System or any other carrier from applying any available technology to any of its services when it makes sense to do so.

Meanwhile developments were underway that will greatly enhance our ability to switch and transmit calls over terrestrial routes. Bell Laboratories engineers have developed a new coaxial cable system with a capacity of 108,000 voice channels. The new communications "superhighway" will far exceed the capacity of the largest system now in use, which carries 32,400 voice channels. The new system will be ready for commercial service in early 1974 over a route between Pittsburgh and St. Louis.

At about the same time we will begin field tests of a transmission system,

"I recall a case where it took a team of operators something like eleven hours to locate a serviceman in Korea so he could take a call about a death in the family. This wasn't an above-the-call-of-duty kind of example. It's their job. But my point is that it was not only their job; they wanted to do it."

Bob Beck, Vice President and General Manager—Western Area, AT&T Long Lines

"The job of forecasting growth is a big one. The type of growth people don't see is growth in data transmission. Industry, of course, is using the telephone more to transmit data of all kinds and this means we have to put in new cable and other facilities. Our circuits are being used increasingly for this purpose and the new plant must be in to handle growth as it occurs."
Charles Hugel, Operating Vice President, New Jersey Bell

known as the millimeter waveguide, which will offer even further advantages—voice-channel capacity up to about 230,000 two-way simultaneous calls, and lower costs.

A new electronic toll switching system scheduled for introduction by early 1976, will handle about 350,000 long distance calls an hour—three times as many as the finest electromechanical toll system now in use anywhere. Moreover, it will take up less space, be easier to maintain, and will provide the flexibilities of stored computer programming.

An increasingly important aspect of Bell Laboratories' work these days has not to do with the development of communications hardware, but with the creation of "software"—i.e., programs, concepts, ideas and techniques that promise significant improvement in our ability to manage business operations that constantly grow in size and complexity.

For example, a computer-programmed approach to the forecasting of future needs for switching equipment provides not only economy and speed but the assurance that our switching centers will more precisely fit the needs of the communities they are designed to serve. Similarly newly developed computer-programmed inventory control systems help us conserve capital by optimizing the utilization of plant facilities.

In another aspect of our operations, a computer-controlled test system provides centralized automatic measurements of trunk circuits throughout an entire metropolitan area, or even an entire state. The measurements check

signal loss and transmission noise, then provide computer print-outs summarizing troubles requiring corrective action. A field trial in the San Francisco Bay area concluded successfully in 1972.

Likewise new techniques and technologies are being applied to the Bell System loop plant, the tree-like network of wires and cables that connect the individual telephone customer to the central office. Attention to the loop plant has increased to meet two trends: an unprecedented increase in the anticipated number of telephone main stations and the increasing movement of customers.

This movement and expansion will be met by new types of cable, new connective systems and terminals, improved loop electronics, a newly designed main distributing frame, more efficient maintenance procedures and stepped-up efforts in planning and administration.

To help reduce the costly changes in the loop plant's network of cables and wires that must be made when telephone customers move, a team from

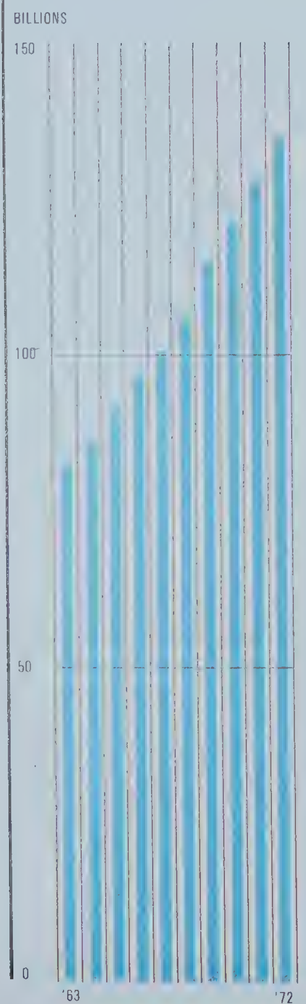
"Western Electric's day-to-day relationship with the Operating Companies helps keep us abreast of customer needs. Our regional organization shortens our lines of communications and improves the speed of our response. I'll bet I talk as many as five times a day with my Telephone Company counterpart to make sure our programs are meeting his needs."
Howard Nilson, General Manager—Southwestern Region, Western Electric

AT&T, Bell Laboratories and several Operating Companies created the Serving Area Concept, or SAC. Now on field trial in several Operating Companies, SAC is a much-improved method of making changes in the wires to individual homes. With SAC, changes in the cable distribution are more efficient, less costly and more convenient.

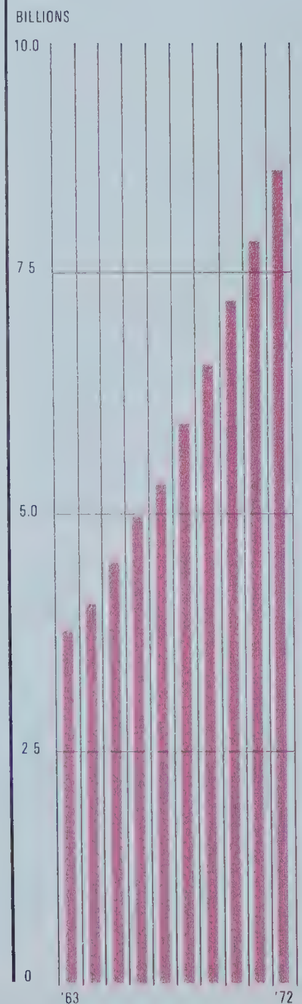
These and other developments are important not only for the efficiencies and cost-savings they provide. Equally if not more important is the fact that our increasing use of computer technology is freeing our management people to do more of what they are paid to do—think and create; use judgment, initiative and imagination; find ways to apply personal consideration in their dealings with customers as well as employees; in short, to manage better.

Another service improvement introduced in 1972 will particularly benefit rural customers and areas of sudden growth. Up to now, individual line service in rural areas has not been the norm, because of the high cost involved. Through an interleaving tech-

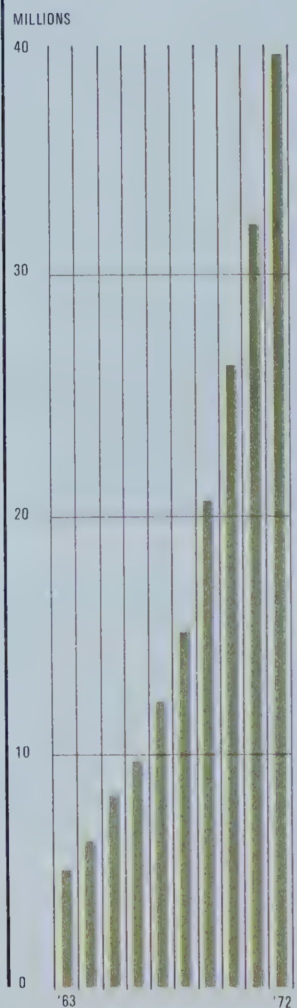
Telephone Conversations
In 1972, the Bell companies handled more calls than ever before—by some seven billion conversations.



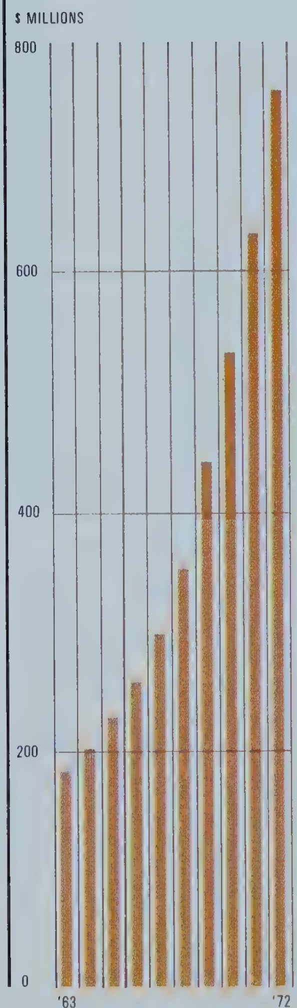
Long Distance Messages
Long distance calls increased by over 10 per cent. In 1972 customers dialed 79 per cent of long distance calls.



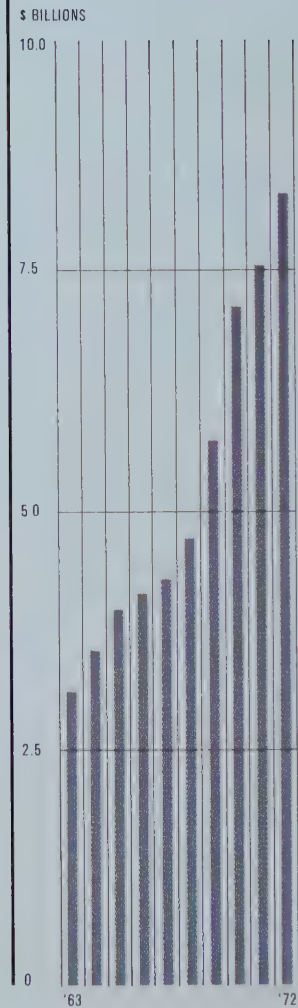
Overseas Conversations
We handled over 20 per cent more overseas calls than in 1971, over 200 per cent more than five years ago.



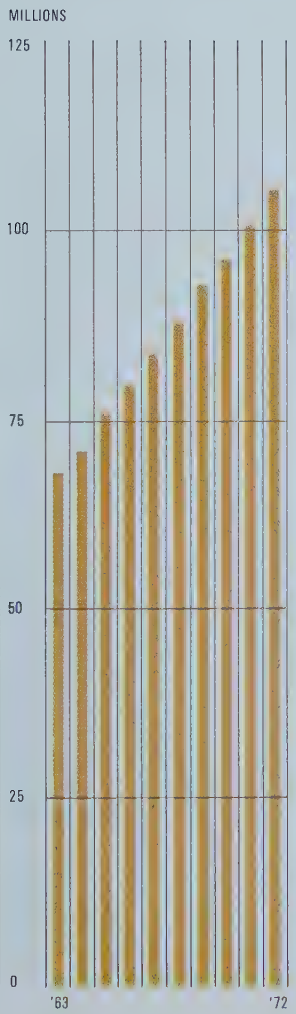
Data Service Revenues
Our data service revenues—from both private line and Dataphone® services—increased by 18 per cent in 1972.



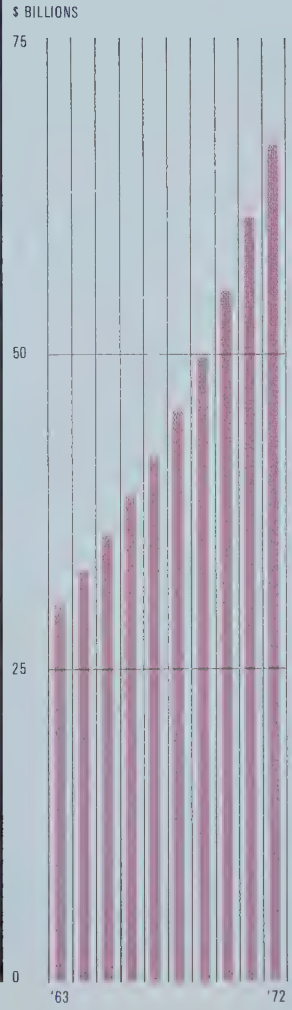
Construction Expenditures
We spent $8.3 billion last year to expand, modernize, move, or replace Bell System facilities.



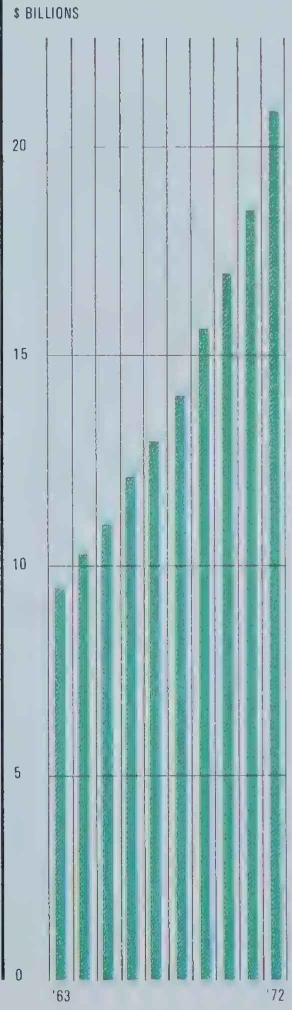
Total Telephones
We gained over five million telephones in 1972—1.2 million more than in 1971.



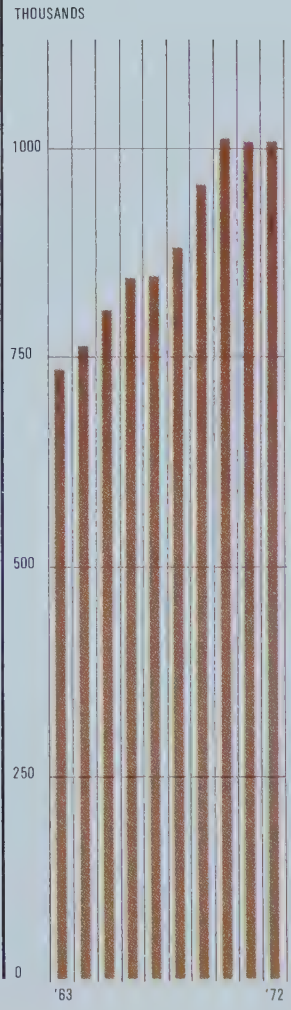
Total Telephone Plant
Our equipment and facilities have more than doubled in the past eight years. Total telephone plant at year's end stood at $67 billion.



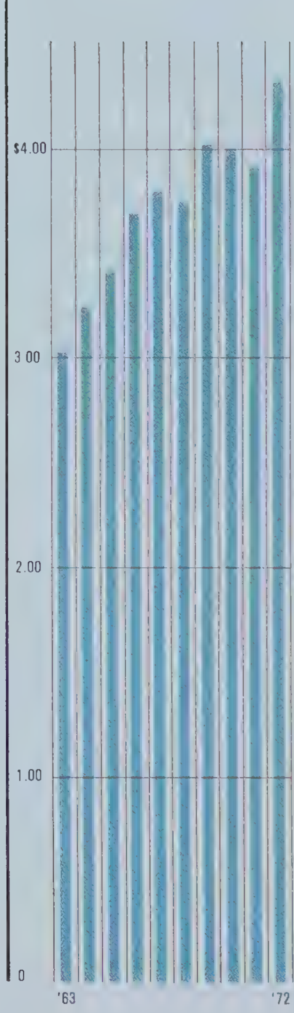
Total Revenues
Bell System revenues in 1972 exceeded $20 billion, reflecting the economy's upturn and necessary rate adjustments.



Total Employees
At year's end the Bell System employed just over 1,000,000 men and women, only a few more than a year ago.



Common Share Earnings
1972 saw a resumption of the improvement in common share earnings that characterized most of the 1960's. Net income applicable to AT&T common shares increased by over 10 per cent.



"Back in the old days, it was a lot simpler for a human being to keep up with records needed for the business. Today there's a whole new order of complexity. This is why we have a new organization to centrally develop a new business information system."

John Coruthers, Assistant Vice President — Business Information Systems, Illinois Bell

nique that combines several simultaneous signals on the same line, a newly developed multiplexing system can serve up to 80 telephone lines using only two cable pairs from a central office, thereby permitting telephone companies to offer more economical individual service or to put fewer customers on each line.

Services for Government

The Federal Government is the largest user of the Bell System's communications services and no customer presents us with more varied and sophisticated requirements. The Federal Telecommunications System, serving the civilian agencies, is today larger than the Bell System's entire interstate network was in 1950. The Autovon network, which the Bell System and a number of independent telephone companies built and now operate for the Department of Defense, incorporates the most advanced transmission and switching facilities, including 51 electronic switching offices, to assure fast, flexible—and secure—communications among military installations throughout the U.S.

Also in 1972, the Western Electric Company continued at the request of the government as prime contractor for the Army's Safeguard antiballistic missile system, an undertaking now reduced in scale as a consequence of the signing of strategic arms limitations agreements by the U.S. and the Soviet Union. As it has for some 20 years, Western Electric's subsidiary, Sandia Corporation, continued opera-

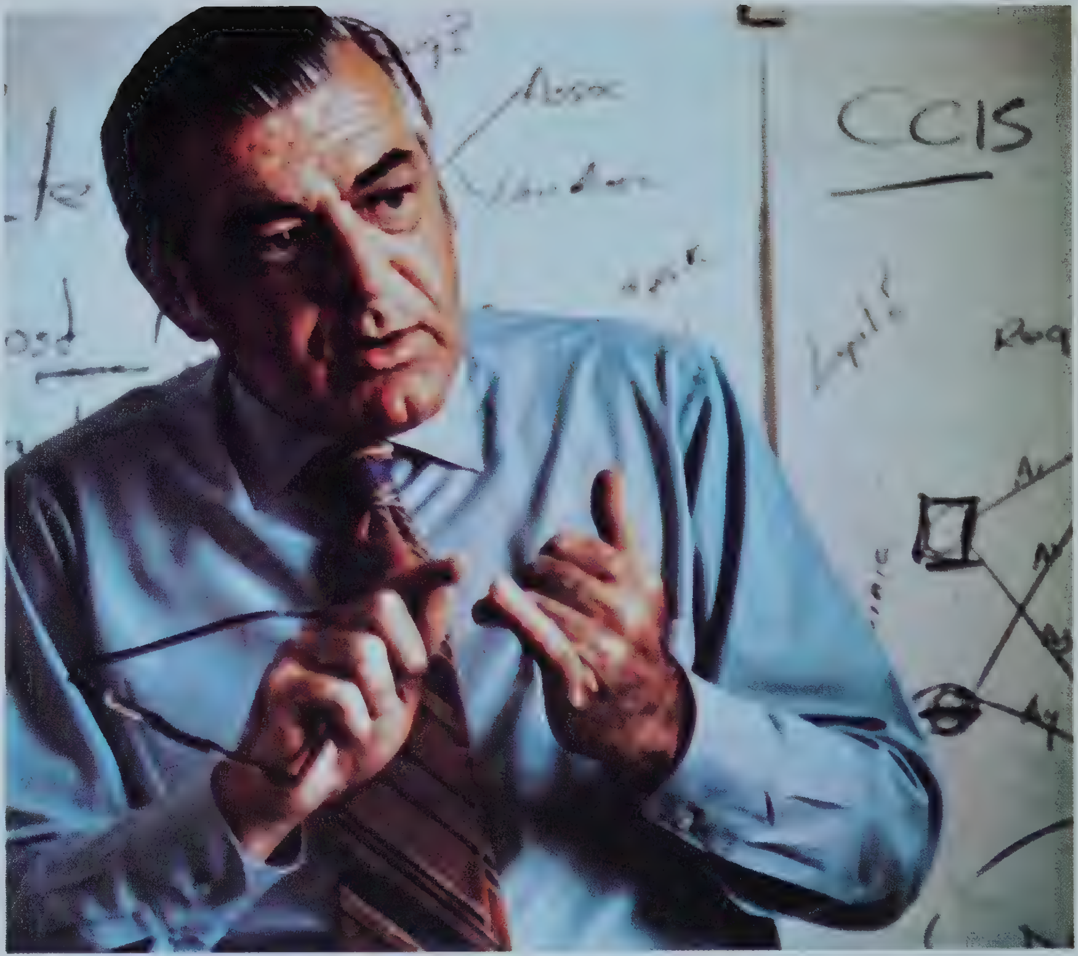
"Bell Labs cannot just consider design and manufacturing costs. It'd be easier if we could. But beyond first costs, we must also consider operating costs. If you don't provide maintenance features, sure, you can cut initial costs. But you pay for your thrift again and again—in testing, in installing, and in hiring the people to service the system once it's in. Besides, service will also suffer."

Eric Sumner, Executive Director—Loop Transmission, Bell Telephone Laboratories

tion of Sandia Laboratories for the Atomic Energy Commission on a no-profit, no-fee basis.

On April 1, 1972, Bellcomm, Inc., a subsidiary of AT&T and Western Electric, was merged with Bell Telephone Laboratories. This was no routine corporate rearrangement. Rather did it mark the successful completion of the mission of an organization altogether unique in the Bell System. Staffed almost entirely by scientists and engineers and comprising no more than 490 employees at its peak, Bellcomm was established in 1962 at the request of the National Aeronautics and Space Administration for the purpose of providing systems engineering assistance to Apollo, the nation's manned lunar flight program.

AT&T's directors took note of Bellcomm's accomplishments in a resolution praising the members of the organization for their "distinguished role in one of history's great technological achievements, reflecting credit on the Bell System and helping to fulfill a major aspiration of the people of the nation and the world."



"Anticipating what technology we'll have available to provide service is a critical element in our long range planning for the future. In this area our bedrock has been and will be Bell Laboratories. Fortunately, Bell Labs has been a leader in technological change, and so the burden is on us to sharpen our planning so as to make the latest technology available, as needed, to do the job."
Joe Bader, Engineering Director—Systems Planning, AT&T

Human Resources

The Bell System began 1972 with 1,000,573 employees, ended it with 1,000,772. That the Bell companies were able to cope with a steady buildup in the volume of business they handled during the course of the year with virtually no increase in employment attests not only to the effectiveness of management efforts to improve productivity but to the growing proficiency of the Bell System's work force. Turnover rates, which had risen to troubling levels in several places—notably some of our larger cities—were lower, reflecting not only economic conditions but intensified efforts to acclimate younger employees to their jobs and equip them to perform to their own as well as to the company's satisfaction.

In the course of the year the Bell companies expanded the application of job enrichment programs to a wider range of jobs. These programs spring from a recognition that there may be limits to the productivity advances that can be accomplished by such traditional methods as work simplification and fragmentation. Now, instead of simplifying jobs, we seek to enlarge them. Instead of fragmenting assignments, we seek to enhance their challenge.

The concept of job enrichment is not new but we know of no other business in which it has been tried—and proven—on such a scale or in so wide a range of occupations. The potential of this approach—both in terms of enhanced performance and employee satisfaction—is perhaps best conveyed —not by statistics, although it can be— but by the observation of a young Indiana Bell employee whose responsibilities had been enlarged from a single repetitive aspect of directory preparation to complete accountability for the directories of three suburban towns: "When I put out the first directory all by myself," she said, "I just —well I just floated. I really felt satisfaction in it."

As a further effort toward assuring equality of opportunity in our business, all the Bell companies in the course of the year adopted revised Affirmative Action Programs specifying the levels of representation of minorities and women they would seek to attain over the years ahead at every level of our business and in every occupation. They also adopted an Upgrade and Transfer Plan aimed at enlarging the scope of opportunity for all employees by facilitating interdepartmental movement for qualified people.

In mid-January, 1973, AT&T and its associated telephone companies reached an agreement with the U.S. Department of Labor and the Equal Employment Opportunity Commission

"The biggest part of what we spend on construction goes to meet the demand for new telephone service—in other words, growth. But meeting the demand for new service or maintaining the old—service is what it's all about. For me, that means being ready with the equipment and the buildings to supply service wherever and whenever our customers expect it."

Marvin Glass, Building Engineer, Pacific Northwest Bell

"We're going to continue to be an attractive business. Demand for communications is booming. We're moving faster to meet that demand with new products, new and better services. Management is younger, more aggressive. Many top officers in their forties. Plenty of drive. I see this as an indication of a more creative, forward-looking response to the demands of the business."
Vicki Bruni, Statistician—Economic and Financial Studies, New Jersey Bell

on a comprehensive program aimed at facilitating the movement of qualified women and minority group members into better jobs. The EEOC has in turn moved to dismiss the case against the Bell companies that it brought before the Federal Communications Commission in December of 1971.

Under this agreement, one-time payments totaling approximately $15 million are going to some 15,000 present employees who may have been delayed in transferring to better-paying jobs. The effect of these payments has been reflected in the 1972 earnings figures contained in this report.

We view this agreement as a further step in the Bell System's continuing efforts to assure equal opportunity throughout our business and to assure that our practices conform to current legal requirements in this rapidly evolving field. Under its terms, qualifications remain, as they must, the fundamental criterion for advancement in the Bell companies. The further expansion of opportunity now afforded and the incentives it inspires will, we believe, strengthen our business'

"We're winning a substantial majority of our competitive cases where we and someone else are bidding for a communications contract. Our advantage is in the quality of our equipment and the responsibility we take for its continuing maintenance. And while other companies may come up with special selling features, if you look at all the costs—especially the long term costs—our successes tell us that we're the best."

William Mobraaten, Vice President—Administration, Pacific Telephone

capability for the long term.

As the press (and our own advertising) has noted, the Bell companies employ a number of male operators and a number of women are employed on outside craft jobs as well. Whether this trend will prove significant, only time and gathering experience will tell. In any case, what should be plain is that we have no male jobs, no female jobs, no black jobs and no white jobs. What counts is the ability to perform the work and a readiness to do one's best.

At the end of the year, minorities accounted for about 13 per cent of total Bell System employment, four per cent of management employment. Women held 28 per cent of management posts.

Down through the years the Bell System has been fortunate in its ability to attract to its ranks a great number of people whose personal commitment to service they express not only on the job but in a wide range of community endeavors. Today more and more of these activities, including those sponsored by the Telephone Pioneers of America, are addressed to the more urgent and seemingly very nearly intractable problems of our times: the problems of our cities and the problems posed for us by the prospect of a deteriorating environment. All across the country Bell System people may be found in the ranks of concerned citizens who devote countless hours they might otherwise devote to themselves to such activities as tutoring potential school dropouts and fighting drug addiction.

In 1972, the Bell companies themselves continued unabated a wide range of programs reflecting their recognition that over the long run the vitality of our business and the vitality of the communities we serve are inseparable. Some of the companies sponsor work-study programs for young people who might otherwise be required to leave school. Some provide business counsel to school administrators. Some sponsor clinics for minority enterprises and some operate day-care centers for the children of employees.

Like their community activities, the companies' contributions programs are diverse. Each is separately administered to meet local needs. Total Bell System contributions in 1972 amounted to $16.2 million.

Organization

From the early years of this century, the Bell System has been well served by the organizing principles established for it by Theodore N. Vail, our business' first general manager and AT&T's president from 1907 to 1918. It is his concept of a nationwide association of companies, each separately managed but all joined in common purpose and sharing common operating procedures, that permits our

business to achieve coordination on a national scale at the same time that it remains responsive to the unique needs of each community it serves.

It is now more than fifty years since Vail relinquished the helm. Thus it is not surprising that today we confront changes in our operating environment unforeseen in his time. In Vail's day, our business served what was still a nation of neighborhoods; today we serve what has become to all intents and purposes one neighborhood. Today—to a degree beyond envisioning in Vail's day—the Bell System network is—because it must be—a single nationwide entity, each of its trillions of parts compatible with all the others. And today our business and the industry of which it is a part confront a range of fundamental policy issues, most of them new in the last decade, requiring that each Bell company take account of the impact of its action on all the others. But for all the changes that have occurred since his time, none contradicts—indeed they confirm—the soundness of the fundamental principle of organization that Vail so firmly stated more than half a century ago. Now more than ever we must be one System.

It was to this end that—almost a year ago and coincident with the announcement of the company's new leadership—AT&T undertook a major restructuring of its headquarters organization. More specifically the aims of this reorganization were threefold:

—to strengthen the coordination of the resources required to give good service.

—to strengthen coordination of the Bell System's relationships with the main constituencies that affect our business: investors, employees and the public at large.

—to strengthen our business' long-range planning capabilities.

Accordingly today AT&T's General Departments are deployed in three major groupings. Reporting to the president are those departments responsible for the company's financial activities and the conduct of its relationships with government, with the public and with employees. Reporting to the vice chairman are those departments responsible for overseeing Bell System operations, assuring the quality of Bell System service and the effective management of the technological resources necessary to provide it. To this end, he oversees the company's interest in the Western Electric Company and Bell Telephone Laboratories. A third grouping, reporting to the executive vice president, is responsible for corporate planning studies, market and service plans and the application of economics and the management sciences to the solution of business problems.

Under the direction of the Chairman, these three officers and the vice president and general counsel comprise AT&T's Executive Policy Committee. It is through this committee that the Bell System sets its course on matters of fundamental corporate policy.

The Executive Policy Committee does not operate in isolation. Indeed, it is explicitly pledged to propose no policy affecting the interest of any or all of the associated companies without full consultation with them.

It is for this purpose that—almost monthly—the Executive Policy Committee meets with the presidents of all the associated companies. Some of these meetings last but one day, some for a full business week. Some are addressed to immediate problems, some to longer-range objectives. All are aimed at making the experience of each of our associated companies available to all of them. Their aim is to take full account of the diverse conditions our companies face and from it to develop the common understanding that will permit our business at one and the same time to achieve national coordination and meet local needs.

Finally, it is in these meetings that the Bell System's goals are set and commitments made to their achievement. It is very largely as a consequence of the determinations made at these meetings and the sharing of those determinations throughout our business that this record of 1972 is one of commitments met and goals achieved.

THE FINANCIAL STATEMENTS on the following pages consolidate the accounts of American Telephone and Telegraph Company and its telephone subsidiaries. These companies maintain their accounts in accordance with the Uniform System of Accounts prescribed by the Federal Communications Commission.

These financial statements have been prepared in conformity with generally accepted accounting principles, which are consistent in all material respects with the accounting prescribed by the Federal Communications Commission, except as to revenue refunds and investments, as discussed in Notes to Consolidated Financial Statements.

Lybrand, Ross Bros. & Montgomery, Certified Public Accountants, have examined these financial statements and their report is shown below. The other auditors referred to in their report are Arthur Young & Company as auditors of Western Electric Company and Southwestern Bell Telephone Company, and Arthur Andersen & Co. as auditors of Illinois Bell Telephone Company.

A. L. Stott
Vice President and Comptroller

Report of Independent Certified Public Accountants

To the Share Owners of American Telephone and Telegraph Company: We have examined the consolidated balance sheet of American Telephone and Telegraph Company and its telephone subsidiaries as of December 31, 1972 and the related statements of income and reinvested earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously examined and reported upon the consolidated financial statements of the Company and its telephone subsidiaries for the year 1971, which have been restated as described in note (b) to the financial statements. The financial statements of two telephone subsidiaries included in the consolidated financial statements (constituting total assets of $8,752,572,000 and $7,960,911,000 and total operating revenues of $3,274,481,000 and $2,968,491,000 included in the consolidated totals for 1972 and 1971, respectively) were examined by other auditors. The consolidated financial statements of Western Electric Company, Incorporated and Subsidiaries, the Company's nonconsolidated subsidiary (which statements reflect net income of $282,941,000 and $258,412,000 included in consolidated net income of the Company for 1972 and 1971, respectively) were also examined by other auditors. The reports of other auditors have been furnished to us and our opinion expressed herein, insofar as it relates to the amounts included in the consolidated financial statements for subsidiaries examined by them, is based solely upon such reports.

In our opinion, based upon our examination and the reports of other auditors and subject to the possible effect, if any, of the proposed income tax regulations referred to in note (d) to the financial statements, the consolidated financial statements on pages 30 to 37 present fairly the consolidated financial position at December 31, 1972 and 1971, the consolidated results of operations and the consolidated changes in financial position for the years then ended of American Telephone and Telegraph Company and its telephone subsidiaries, in conformity with generally accepted accounting principles applied on a consistent basis.

LYBRAND, ROSS BROS. & MONTGOMERY

1251 Avenue of the Americas, New York, N.Y.
February 9, 1973

	Thousands of Dollars	
	Year 1972	Year 1971 (b)
OPERATING REVENUES		
Local service	$10,362,884	$ 9,135,486
Toll service	9,771,433	8,632,842
Miscellaneous	908,718	828,137
Principally from directory advertising		
Less: Provision for uncollectibles	138,923	154,333
Total operating revenues	20,904,112	18,442,132
OPERATING EXPENSES		
Maintenance	4,293,806	3,776,617
Depreciation	3,041,726	2,764,240
Portion of the cost of depreciable plant charged against current operations		
Traffic	1,668,831	1,586,748
Costs, principally operators' wages, incurred in the handling of messages		
Commercial	720,180	646,515
Primarily costs of local business office operations		
Marketing	895,050	806,766
Accounting	606,508	555,078
Research and fundamental development	149,362	133,963
Provision for pensions and other employee benefits (c)	1,510,668	1,221,957
Other operating expenses	1,028,861	900,214
Less: Expenses charged construction	396,774	317,501
Total operating expenses	13,518,218	12,074,597
Net operating revenues *(carried forward)*	$ 7,385,894	$ 6,367,535

For notes, see pages 35 through 37

	Thousands of Dollars	
	Year 1972	Year 1971 (b)
Net operating revenues *(brought forward)*	$7,385,894	$ 6,367,535
OPERATING TAXES		
Federal income (d)	1,669,913	1,433,131
State, local and social security	2,136,823	1,880,698
Total operating taxes	3,806,736	3,313,829
Operating income	3,579,158	3,053,706
OTHER INCOME (e)	447,917	436,707
Income before interest deductions	4,027,075	3,490,413
INTEREST DEDUCTIONS	1,495,017	1,288,382
NET INCOME (d)	$ 2,532,058	$ 2,202,031
EARNINGS PER COMMON SHARE (d) *based on average common shares outstanding, 549,501,000 in 1972 and 549,304,000 in 1971, after recognition of preferred dividend requirements of $145,730,000 for 1972 and $48,830,000 for 1971.*	$4.34	$3.92
REINVESTED EARNINGS		
At beginning of year as previously reported	$10,615,162	$ 9,879,267
Adjustment for revenue refunds (b)	37,666	—
As restated	10,577,496	9,879,267
Add—Net Income	2,532,058	2,202,031
	13,109,554	12,081,298
Deduct—Dividends declared:		
Preferred	149,765	57,984
Common—1972, $2.70 per share; 1971, $2.60 per share	1,483,146	1,428,191
Miscellaneous—net	949	17,627
	1,633,860	1,503,802
REINVESTED EARNINGS AT END OF YEAR	$11,475,694	$10,577,496

ASSETS	Thousands of Dollars December 31, 1972	December 31, 1971 (b)
TELEPHONE PLANT—at cost		
Land, buildings and equipment		
In service	$63,920,261	$57,615,595
Under construction	3,086,288	2,878,235
Held for future use	75,707	74,124
	67,082,256	60,567,954
Less: Accumulated depreciation	14,482,348	13,370,886
	52,599,908	47,197,068
INVESTMENTS (f)		
At equity	3,118,431	3,112,363
At cost	108,832	148,122
	3,227,263	3,260,485
CURRENT ASSETS		
Cash and temporary cash investments—less drafts outstanding: 1972, $271,441,000; 1971, $213,732,000 (g)	1,086,346	922,752
Receivables—less allowance for uncollectibles: 1972, $28,334,000; 1971, $30,578,000	2,737,742	2,318,430
Material and supplies	337,987	313,541
Prepaid expenses	128,376	102,560
	4,290,451	3,657,283
DEFERRED CHARGES	507,423	404,499
TOTAL ASSETS	$60,625,045	$54,519,335

For notes, see pages 35 through 37

LIABILITIES AND CAPITAL	Thousands of Dollars December 31, 1972	December 31, 1971 (b)
EQUITY		
American Telephone and Telegraph Company		
Preferred shares—par value $1 per share		
Authorized 50,000,000 shares		
$4 Convertible preferred shares—at stated value $50 per share (h)	$ 1,373,008	$ 1,373,158
Outstanding at December 31, 1972, 27,460,000 shares		
$77.50 Preferred shares—at stated value $1,000 per share (i)	625,000	—
Outstanding at December 31, 1972, 625,000 shares		
Common shares—at par value $16⅔ per share (h) (j)	9,228,572	9,155,163
Authorized 750,000,000 shares		
Outstanding at December 31, 1972, 553,714,000 shares		
Premium on shares	5,449,011	5,300,752
Proceeds in excess of preferred stated value and common par value		
Reinvested earnings—*see page 31*	11,475,694	10,577,496
	28,151,285	26,406,569
Minority interests (j)	736,650	843,628
	28,887,935	27,250,197
DEBT (k)		
Long and intermediate term	24,143,326	21,228,326
Interim—notes payable	1,876,319	1,600,010
	26,019,645	22,828,336
CURRENT LIABILITIES		
Accounts payable	1,636,553	1,479,313
Advance billing and customers' deposits	528,336	464,367
Dividends payable	438,941	397,142
Taxes accrued	961,294	698,351
Interest accrued	413,910	347,013
	3,979,034	3,386,186
DEFERRED CREDITS		
Unamortized investment tax credit	874,496	644,436
Deferred income taxes	832,318	389,451
Other	31,617	20,729
	1,738,431	1,054,616
TOTAL LIABILITIES AND CAPITAL	$60,625,045	$54,519,335

Consolidated Statements of Changes in Financial Position

	Thousands of Dollars	
SOURCE OF FUNDS:	Year 1972	Year 1971
From Operations		
Net Income	$ 2,532,058	$ 2,202,031
Add—Expenses not requiring funds:		
Depreciation	3,041,726	2,764,240
Deferred income taxes	442,867	275,093
Investment tax credit—net	230,060	53,142
Less—Income not providing funds:		
Interest charged construction	208,718	206,053
Share of the income, after dividends, of companies accounted for on an equity basis	136,782	132,104
Total funds from operations	5,901,211	4,956,349
From Financing		
Issuance of shares *(principally preferred)*	846,518	1,379,981
Issuance of long and intermediate term debt	2,950,000	3,180,000
Change in interim debt—net	276,309	(605,325)
	$ 9,974,038	$ 8,911,005
APPLICATION OF FUNDS:		
Telephone plant	$ 8,081,514	$ 7,205,042
Dividends	1,632,911	1,486,175
Change in minority interests	106,978	(45,352)
Change in deferred charges	102,924	45,858
Repayment of long-term debt	35,000	200,000
Change in cost of investments	(17,490)	56,391
Change in working capital	40,320	(52,279)
Other—net	(8,119)	15,170
	$ 9,974,038	$ 8,911,005

The change in working capital is accounted for by:	Year 1972	Year 1971
Increase in current assets:		
Cash and temporary cash investments, net of drafts	$ 163,594	$ 50,142
Receivables	419,312	131,703
Material and supplies	24,446	25,912
Prepaid expenses	25,816	10,481
	633,168	218,238
Increase (decrease) in current liabilities:		
Accounts payable	157,240	168,609
Advance billing and customers' deposits	63,969	40,739
Dividends payable	41,799	28,000
Taxes accrued	262,943	(30,231)
Interest accrued	66,897	63,400
	592,848	270,517
Change in working capital	$ 40,320	$ (52,279)

Notes to Consolidated Financial Statements

(a) **Accounting Policies**—The financial statements reflect the application of certain accounting policies described in this note. Other policies and practices are covered in notes (c) and (g).

Consolidation — The consolidated financial statements include the accounts of the American Telephone and Telegraph Company and its telephone subsidiaries. All significant intercompany transactions are excluded from these statements except as discussed below under *Purchases from Western Electric*. The investment in Western Electric Company, Incorporated, an unconsolidated subsidiary, and certain other investments (where it is deemed that the Company's ownership gives it the ability to exercise significant influence over operating and financial policies) are carried at equity. All other investments are carried at cost.

Purchases from Western Electric — Most of the telephone equipment, apparatus and materials used by the companies consolidated has been manufactured or procured for them by Western Electric Company. Contracts with the telephone companies provide that Western's prices to them shall be as low as to its most favored customers for like materials and services under comparable conditions. The consolidated financial statements reflect items purchased from Western at cost to the companies, which cost includes the return realized by Western on its investment devoted to this business.

Depreciation—Provision for depreciation (5.2% in 1972 and 1971 of the cost of depreciable plant in service) is based on straight-line composite rates. Depreciation for income tax purposes is determined on different bases and methods as explained under *Income Taxes* below.

Income Taxes:

(1) Under various accelerated depreciation provisions of the tax law, depreciation for income tax purposes on plant placed in service after 1969 is greater than the straight-line depreciation provided in the accounts. Provision is made ("normalization") for the deferred income taxes resulting from the use of accelerated depreciation and is included in income tax expense ($438,402,000 in 1972 and $272,869,000 in 1971). Also see note (d).

(2) The companies have consistently followed the practice of deducting for income tax purposes certain taxes and payroll-related construction costs which are capitalized in the financial statements. In addition, interest charged construction is excluded from taxable income. The resulting effect on income taxes, to the extent it is not offset by a related reduction in depreciation expense for tax purposes, is reflected in net income. In recent years deductions and exclusions for tax purposes which are related to construction costs have increased, resulting in lower income taxes in relation to net income.

(3) Investment tax credits have been deferred and are being amortized by credits to operating income over the life of the plant which gave rise to the credits.

Research and Fundamental Development — Basic research and fundamental development costs are expensed currently. The cost of specific development and design work incurred by Western Electric Company is related to products manufactured and is included in the cost of such products.

(b) **Revenue Refunds**—The financial statements for 1971 have been adjusted to recognize the effect of revenue refunds in California, Virginia, and West Virginia as a result of regulatory and court orders in those states. Amounts applicable to 1970 and 1971, net of income tax, were charged directly to reinvested earnings in the books of account in 1972 (under accounting prescribed by the Federal Communications Commission); however, in accordance with generally accepted accounting principles, the income statement for 1971 has been restated and the opening balance of reinvested earnings for 1972 has been adjusted. Such restatement reduced 1971 net income by $37,666,000 ($.07 per share).

(c) **Provision for Pensions and Death Benefits** — The Company and its consolidated subsidiaries have non-contributory plans covering all employees and providing for service pensions and certain death benefits. These companies have

accrual programs under which actuarially determined regular payments are made to trust funds that are irrevocably devoted to service pension and death benefit purposes. The total provision for these service pensions and death benefits, including amounts charged to construction, was $986,319,000 in 1972 and $779,871,000 in 1971. Amendments to the Plan on June 1, 1971 and October 1, 1971 provided for improved benefits and resulted in increased pension accruals beginning October 1, 1971. The cost of these changes was about $184,592,000 in 1972 and $43,711,000 in 1971.

(d) **Depreciable Lives of Certain Plant for Income Tax Purposes**—In income tax returns for the year 1971 the American Company and its telephone subsidiaries adopted for income tax purposes shorter depreciation lives than those used for book purposes for certain plant, as allowed in proposed income tax regulations of the Treasury Department. If the regulations become final in their proposed form without normalization, or normalization is not otherwise provided, and with respect to 1972 if the Company and its telephone subsidiaries adopt similar shorter-life provisions of the proposed regulations in filing income tax returns for the year 1972, net income would be increased for the years 1972 and 1971 by about $108,600,000, and $88,000,000 ($.20 and $.16 per share), respectively. There can be no assurance that such effect on net income will occur considering that departure from normalization of income taxes would be inconsistent with recent Congressional policy on like matters.

(e) **Other Income**—Includes principally the proportionate interest in earnings of companies, the investment in which is carried on the equity basis, of $294,135,000 in 1972 and $274,513,000 in 1971; interest charged construction of $208,718,000 in 1972 and $206,053,000 in 1971; less minority interests in net income of subsidiaries of $72,985,000 in 1972 and $63,421,000 in 1971.

(f) **Investments**—Investments at equity as of December 31, 1972, with dollars expressed in thousands, comprise:

			Equity			
Company	Percent Ownership	Market Value[2]	Shares at Cost[3]	Excess of Net Assets Over Cost	Advances	Total
Western Electric Company, Incorporated[1]	100.0	$ —	$1,326,001	$1,579,047	$ —	$2,905,048
The Southern New England Telephone Company	17.1	73,409	47,562	21,560	13,700	82,822
Bell Telephone Laboratories, Incorporated	50.0[4]	—	79,000	—	—	79,000
Cincinnati Bell, Incorporated	25.7	40,368	24,345	15,390	8,200	47,935
All Other	—	—	871	2,750	5	3,626
			$1,477,779	$1,618,747	$21,905	$3,118,431

[1]Total assets and liabilities of Western Electric Company, Incorporated and its Subsidiaries at December 31, 1972 were $4,309,899,000 and $1,404,851,000, respectively. Net income for 1972 was $282,941,000.
[2]Where applicable, based on N.Y. Stock Exchange closing price for 1972.
[3]The Uniform System of Accounts of the Federal Communications Commission requires that investments be carried on the books of the companies at cost. In accordance with generally accepted accounting principles, certain investments are included at equity in the accompanying balance sheets. See note (a), *Consolidation*.
[4]Western Electric Company, Incorporated, owns the other 50.0 per cent of Bell Telephone Laboratories, Incorporated.

Investments at cost include $57,915,000 ($185,328,000, based on 1972 year-end closing price on the N.Y. Stock Exchange) relating to Communications Satellite Corporation (Comsat). The Company owns 29% of the voting stock of Comsat and has representation on the Board of Directors. However, the equity method of accounting for this investment is not deemed appropriate because the Company is precluded from exercising significant influence over operating and financial policies of Comsat under terms of the enabling legislation establishing Comsat.

(g) **Cash and Temporary Cash Investments**—Cash and temporary cash investments have been reduced by the amount of drafts outstanding with a corresponding reduction in accounts payable. It is the practice of the Company and some telephone subsidiaries to make certain payments by draft and to record such drafts as accounts payable until such time as the banks honoring the drafts have presented them for payment. The Company maintains cash and temporary cash investments not only to meet its own obligations but to maintain funds upon which the subsidiary companies may draw on a day-to-day basis.

(h) **Convertible Preferred Shares**—Each $4 preferred share can be redeemed by the Company at a premium of $1 per $50 share commencing August 1, 1974 and at diminishing amounts thereafter, and is convertible into approximately 1.05 common shares of the Company. During 1972, 2,995 shares were converted into 3,153 common shares.

(i) **$77.50 Preferred Shares**—Such shares may be redeemed by the Company at a premium of $75.30 per $1,000 share before January 31, 1974 and at diminishing amounts thereafter. These shares are subject to systematic redemption without premium commencing February 1, 1978.

(j) **Common Shares**—In December 1972 the Company issued 4,396,092 common shares in connection with an exchange offer made to shareowners of the New England Telephone and Telegraph Company. The excess of the fair market value of the Company's shares over the book value of the New England shares tendered amounted to $37,367,000 and is reflected as a deferred charge on the consolidated balance sheets and will be amortized as a charge to net income on the consolidated income statements over a fifteen year period beginning in 1973.

At December 31, 1972 warrants were outstanding to purchase 31,337,622 common shares of the Company, at $52 per share, at any time through May 15, 1975. Warrants to purchase 5,315 shares were exercised during 1972.

(k) **Debt**—Interest rates and maturities on long and intermediate term debt outstanding at December 31, 1972, in millions of dollars, were as follows:

Maturities	2⅝% to 3⅞%	4% to 6⅞%	7% to 9⅜%	Total
1973-1979	$ 835	$1,125	$ 375	$ 2,335
1980-1989	2,480	583	75	3,138
1990-1999	642	3,497	450	4,589
2000-2012	—	4,612	9,469	14,081
	$3,957	$9,817	$10,369	$24,143

The above table includes $35 million 2¾% mortgage bonds due February 1, 1973 which have been refinanced and $150 million 3⅜% debentures due December 1, 1973, which will be refinanced.

Notes payable consist of borrowings from banks and commercial paper, due twelve months or less from date of issue. At December 31, 1972 the average rate of interest on these notes was 5.7%.

Since December 31, 1972 five subsidiaries have announced their intention to sell $1,075,000,000 of long and intermediate term debt. The proceeds of such sales will be applied toward repayment of debt and for general corporate purposes, including extensions, additions and improvements to plant.

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2 William L. Lindholm
3 Robert D. Lilley
4 Edward W. Carter
5 Catherine B. Cleary
6 William M. Batten
7 J. Victor Herd
8 William B. Murphy
9 Edward B. Hanify
10 Archie K. Davis
11 H. I. Romnes
12 Jerome H. Holland
13 Jay Taylor
14 Lloyd D. Brace
15 J. Irwin Miller
16 James R. Killian, Jr.
17 William J. McGill
18 Thomas F. Patton
19 William A. Hewitt

See following page for complete list of Officers and Directors, and Directors' affiliations.


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